Protecting Creditors and Investors -
Capital Maintenance in the European Private Company

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Table of contents

PART I

1 Outline and Focus

1.1 Introduction

The subject of this article is the regulation of capital maintenance in the European Private Company (SPE) proposed in the European Union. The primary reference for the article is the Proposal for a Council Regulation on the Statute for a European Private Company (COM (2008) 396) and its chapter IV on Capital. The article seeks to analyse the capital regime that an SPE will be subject to.

The article is organized in three separate parts. Part I introduces its subject and focus in addition to setting up a set of success criteria for the legislation. Part II goes on to handle the different types of capital maintenance provisions, using use-cases and research on the SPE for each category, with an analysis of the SPE provisions' compatibility with their purpose and criteria of success. Finally, Part III goes on to analyze the regulation of capital as a whole, discussing its appropriateness.

If adopted, the legislation on a European Private Company will look very different from the initial Commission proposal. This article will also cover the proposed amendments of the European Parliament. Finally it considers various proposed amendments in the Council's Working Party on Company Law currently debated, with a particular focus on the negotiations that have taken place during autumn of 2009.

In handling particular SPE provisions, separate mention will be made of the Commission's proposal, the European Parliament amendments and the currently negotiated Working Party proposals. The information provided on the ongoing negotiations within the Working Party is based on public documents, e-mail and phone correspondence and several interviews conducted in Brussels during autumn 2009.[1]

In order to capture the essence of the SPE's capital regulation and understand how it might play out on a continent with various other company forms, this article will employ use-cases[2] depicting different European countries' capital maintenance legislation. The use-cases will show the corresponding provisions of the SPEs that are employed in given Member States. The chosen use-case company legislations regulate private limited liability companies like the SPE. They represent different legal directions and some of them are among the most widely used company forms in Europe. Additionally, a use-case of the 2nd Council Directive is employed.

1.2 Delimitations

The capital maintenance provisions that will be covered are those concerning:

- The structure of a company's capital (Section 6)
- The increase of a company's capital (Section 7)
- The reduction of a company's capital (Section 8)
- The acquisition of a company's own shares (Section 9)
- The distribution of a company's capital (Section 10)
- The maintenance of a company's capital and equity (Section 11)

Unfortunately, due to the scope restrictions on this article, it will not be possible to cover more than the essence of these provisions. There are several institutes of law that deserve a more profound consideration in relation to capital maintenance, some of which are given

[1] See List of References
[2] A 'use-case' defines behavior … by describing the behavior of a system from a user's standpoint, providing a functional description of a system and its major processes (http://tinyurl.com/yhqxxp7, accessed 18.11.2009).

mention in the following. However, the provisions chosen are the ones most relevant to the SPE and fully enable a thorough analysis of its capital regulation.

Tax and accounting law, insolvency law and directors' liability upon breach of capital maintenance provisions are very much important to a company's handling of its capital, but will not be covered in this article primarily because an SPE in this regard will be subject to applicable national law from the Member State in which it is registered.

Regulation on the transfer or withdrawal of shares is not covered due to the article's restricted size. However, the redemption of shares is subject to some attention as it is often used to distribute capital out of a company. Financial assistance on the acquisition of a company's own shares is not covered as the SPE will leave this to applicable national law.

1.3 Definitions

The following terms require definition. Capital maintenance itself is covered in section 3.

1.3.1 Member States

By 'Member States' this article primarily refers to the 27 EU-member states represented in the European Council. When referring to countries affected by the Regulation, 'Member States' also reflect the EEA/EFTA-states (Norway, Iceland and Liechtenstein).

1.3.2 The Regulation

By '(the) Regulation' this article refers to the complete set of provisions regulating an SPE, often meaning the potential final Council regulation.

1.3.3 The Compromise

By '(the) Compromise' this article refers to Council Document 17152/08 of December 11^{th} 2008. This is a compromise proposal drafted to facilitate negotiations in the Working Party on Company Law, based on their previous discussions.

1.3.4 Qualified Majority

Unless otherwise specified, the term 'qualified majority' means that a majority of 2/3 of the voting rights making a decision are in favour of a given result. I.e. if a decision requires a qualified majority, it must have the support of 2/3 of the voting rights present.

2 The European Private Company

2.1 Background of the Proposal

On June 27th 2008 the European Commission submitted its proposal on a Statute for a European Private Company (SPE), COM (2008) 396. The Statute provides for a limited liability company entity that can be created and operated according to the same uniform principles in all EU Member States. It is a key part of the Small Business Act for Europe, COM (2008) 394, a set of initiatives aimed at facilitating Small and Medium Enterprises (SMEs) within the Single Market.

The SPE proposal is especially designed to fit the needs of entrepreneurs and SMEs, however no suggestion has been made to restrict the size of an SPE. It aims to reduce compliance costs on creation and operation of businesses due to the many differences in national company law. Hence, an SPE will follow the same law provisions in any Member State it chooses to operate in. This might be very beneficial to entrepreneurs, but also larger companies wishing to establish branches or subsidiaries within the Single Market. In a 2007 survey conducted by the European Business Test Panel (EBTP) with 462 companies 56% said uniform rules for European Union companies would be useful to them.[3]

According to the Commission's original proposal, 99% of European companies are SMEs, of which only 8% do cross-border business. It is the proposal's intent to serve as an incentive for more companies to pursue cross-border business, by providing SMEs with

[3] EBTP, 'European survey on European Private Company' (2007)

better access to the Single Market. The Commission acknowledges that most SMEs start out nationally; meaning a cross-border requirement for SPEs would prevent many potential cross-border businesses from choosing the company entity. Therefore, the Commission proposes the SPE should also be available to companies that operate solely in one Member State. This represents a change of direction from the European Company (SE) which in order to exist must do business in several Member States.

Due to Centros (ECJ C-212/97) any company may have its registered office in one Member State, only to conduct its business in another, as a result of the freedom of establishment in the EC treaty. This enables foreign companies to be established for the purpose of operating in other Member States, subject to the provisions of foreign company law, and has provided more and more Ltds operating within the Single Market. Although flexible instruments like the Ltd are available to SMEs across the Single Market, the Member States in which they operate are not necessarily familiar with UK company law, creating difficulties in the course of business for foreign companies.

In many Member States, foreign companies are often assumed to be established to circumvent the more familiar national law, resulting in a bad reputation for foreign companies. With a common company entity known throughout the Single Market, Member States avoid the problem of handling foreign law and the SPE might be perceived as a more serious corporate entity. In the EBTP survey about half of the companies indicated that the SPE would address the problem of lack of trust in foreign legal forms.

2.2 The Proposal's Legislative History

Similar to what is the case for the SE; the Statute for a European Private Company will be made in accordance with the EC Treaty Article 308. The final Regulation will not be decided in co-decision between the Council and the European Parliament. Instead it is subject to unanimous decision by the European Council, which shall hear and consider the European Parliament's opinion on the matter.

2.2.1 The Commission's Proposal

The Commission's proposal was met with encouragement by many Member States and seemed to provoke others. It proposes a company form that may operate in any Member State without doing cross-border business, having a minimum share capital of only € 1, with distributions being restricted only by a balance-sheet test. It further implies that the real-seat theory shall not apply,[4] and that an SPE may organize itself as it wishes in its articles of association. All in all, it is a very liberal proposal.

2.2.2 The Parliament Amendments

On March 10th 2009 the European Parliament adopted a legislative resolution on the SPE.[5] The resolution approved of the Commission's proposal, but suggested several amendments, many of which were political compromises to ensure all delegations found the proposal edible. Dr. Sebastian Kuck, assistant to rapporteur Klaus-Heiner Lehne (MEP), explained that the European Parliament were trying to amend the proposal so that the Council negotiations would go more smoothly, e.g. by adding a somewhat fictional cross-border business requirement.[6]

Representatives in the Council's Working Party on Company Law (Working Party) reveal that the European Parliament's opinion has mostly been referenced to strengthen and support Member States' arguments; the suggested amendments have not served as the basis of any discussion. The amendments are covered more thoroughly in Part II of this article.

2.2.3 The Compromise Negotiations

Ever since the Commission presented its proposal it has been subject to debate in the Working Party. The Working Party is led by the current EU Council Presidency, meaning the negotiations have so far been led by three different countries.

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[4] Michel Menjucq implies that the real-seat theory has no place in future company law, see 'Perspectives in Company Law and Financial Regulation' (2009) pp. 124-131.

[5] P6_TA-PROV(2009)0094 (http://tinyurl.com/yhqwrhw, accessed 18.11.2009)

[6] Interview with Sebastian Kuck (06.10.2009)

The French Presidency (July 1st – December 31st 2008) expressed in its Work Programme (1.3. An innovative and competitive Europe) that 'The Presidency particularly aims to work ... on integrating the internal market to the advantage of SMEs by adopting the idea of the European Private Company…', and the French did in fact get the process started. However, the negotiations stalled and a compromise was not in place by the end of their Presidency. In a progress report of November 27th 2008 the Presidency stated that there was disagreement on the cross-border component, labour representation, the company seat and the minimum share capital.[7] These are roughly the same issues being discussed in the Working Party autumn 2009.

The Czech Presidency (Jan 1st – June 30th 2009) were less ambitious with their Work Programme statement on page 6: 'The Presidency will continue to discuss the proposal for a Council Regulation on the Statute for a European Private Company …'. With the Parliament coming into play the Working Party seemed to fall silent. In a progress report of May 8th 2009 the Presidency expressed that issues in need of further discussion were, in particular, employee participation, a cross-border component, the minimum share capital and adequate safeguards and the duties of directors.[8]

This autumn the Swedish Presidency has pushed for the SPE and many believe the legislation is closing up on judgment day. The Commission has signalized they will no longer push for it unless the Swedish Presidency succeed in finding a compromise[9], and representatives in the Working Party indicate that there is less and less interest among Member States to carry the proposal forward. There is a Council meeting scheduled for December 4th 2009 which according to Rolf Skog (Desk Officer of the Working Party) is where a compromise must be made if it is to happen under the Swedish Presidency.

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[7] Council Document 16400/08 DRS 74 SOC 733

[8] Council Document 9658/09 DRS 41 SOC 316

[9] Interview with Judit Fischer (09.10.2009)

Several compromise proposals have been drafted by the Presidencies since the Commission's proposal in June 2008. The proposals and debates have especially differed on worker's participation rights, the seat of the company and the minimum share capital. When it comes to other capital maintenance regulation than the share capital requirement, Member States seem to have grown comfortable with solutions close to those of the Commission. The different options currently on the table and the contents of the current texts when it comes to capital will be more thoroughly covered in Part II of this article.

3 Capital Maintenance

Regulation of the capital within companies is used to protect different interests. Limited liability companies are treated as separate entities from their shareholders. As a result of this the company needs be responsible itself for its liabilities. In order for this responsibility to be of actual importance, there is a need for regulation limiting the possibility of making the company less able to pay its dues.

An important aspect of such regulation is creditor protection. Creditor protection rules pose as barriers to withdrawing money from a company to a creditor's disadvantage. They may also indicate how money should be put into a company, and pose minimum capital requirements. A certain amount of protection of creditor interests is adamant for their interest in supporting businesses, and ensures that their information on a company's situation remains reliable. However, many creditors still protect themselves the best by means of contract.[10]

Another important purpose of capital protection rules is investor protection, especially for minority shareholders. It is important for smaller stakeholders in a company that their

[10] For a more thorough discussion on different creditor protection, see Merkt, 'Creditor Protection and Capital Maintenance from a German Perspective', (2004) 15 EBLR and Payne, Smith, 'Legal Capital and Creditor Protection in UK Private Companies', 5(5) ECL.

interests are not trampled on by majority shareholders, and they are often given rights to protect these interests. For instance, certain decisions within a company may require a qualified majority or unanimous consent. Also, minority shareholders may often call for independent opinions or investigations when their interests are at stake.

The different set of rules can be divided into two categories: Regulation of capital going into the company and Regulation of capital going out of the company. The first category consists mostly of rules about the share capital, capital increases and the company's equity. The second category consists of regulation on distributions, acquisitions of own shares and capital reductions. Obligations of directors to act in accordance with a company's best interests also somehow limit the extent of which capital may exit a company. In Part II these categories will constitute the structure of this article.

There are other types of regulation that builds to the framework of a company's capital. More detailed descriptions of directors' liability and insolvency law pose barriers to the actions of a company, as does the laws on taxation. The categories primarily handled in this article have been chosen as they constitute the fundamental capital rules of the SPE, which are to be analyzed by means of a comparative analysis based on typical European company law. As such, the article does not seek to portray the entirety of capital regulation in any of the legal systems presented; rather it gives an introduction to their basic capital maintenance regulation.

4 Success Criteria

4.1 Criteria

If the Statute for a European Private Company is adopted it will most likely include a provision about a review of the Regulation's application (Art 47 in the proposal), within five years from its implementation. This chapter provides suggestions to which criteria must be met (also in a capital maintenance perspective) in order for such a review to find the Regulation and its implementation successful. This will provide the article with a further elaboration of the research question as set out above in section 1.

4.2 Making the SPE Attractive

4.2.1 Tailoring Conditions for Small and Medium Enterprises

In the explanatory memorandum of COM (2008) 396 the Commission expresses several of the underlying intentions of the SPE proposal. It would be natural to interpret these intentions as future criteria of success for a potential legislation. Hence, in order for the Regulation to succeed it should be congruent with the Commission's expressed goals and provide provisions that allow for companies to be created and operated better than with national law. For the SPE this means having the best possible provisions for Small and Medium Enterprises.

Minimum capital requirements should not be very rigid, allowing for entrepreneurs to start out small. There should be easy access to a capital increase as long as shareholder rights are not compromised. The way of distributions, capital reductions and acquisitions of own shares should reflect that creditors have the power of contract to safeguard themselves, unless their claims are at stake, then the creditors should be given a right to object. The smaller companies, the less need for legislative creditor protection, as the companies will seldom be able to negotiate better terms with creditors than what market demand implies.

In general the capital maintenance regulation should ensure that funds are easily available to companies and not tied up without purpose. However, to the extent that companies might do harm to the interests of their minority shareholders and creditors, the provisions on capital should safeguard against such actions. In balancing the interests of creating a flexible instrument for smaller business and protecting its stakeholders against abuse, the Regulation should opt for solutions that are less complex and require less comprehensive action by the companies. That way the Regulation is simple, predictable and more cost-efficient to SMEs.

4.2.2 Cost-efficient Creation and Operation

The memorandum further states that it 'aims to reduce compliance costs on the creation and operation of businesses …' especially by providing a uniform set of rules for SPEs in all Member States. In order to reduce costs the Regulation should be easy to understand and provide simple methods of conducting a company's business. By allowing companies to organize themselves freely and have flexible provisions on resolutions (e.g. no requirement for physical general meetings), SMEs will be able to conduct their business cost-efficiently.

However, with substantial parts of company regulation left to a company's articles of association, a company will have to develop thorough regulation themselves, representing significant costs. As a result of this there has been much discussion on the development of a set of model articles for the SPE. On July 23rd 2008 the Commission presented a set of model articles to the Working Party providing examples on mandatory and permitted provisions.[11]

As of today, the negotiations in the Working Party imply Member States will be free to offer national model articles for companies to use, without these articles being compulsory. There is no mention of this in the compromise proposal of December 11th 2008, but it is said to be in the preface of the latest proposal. There will not be an official set of European model articles, as such a set could not be agreed upon.[12]

4.2.3 Conceptions of the SPE

4.2.3.1 Predictability

The further the negotiations in the Working Party develop, the more legislation is left to applicable national law. It is difficult to foresee what is left of the Regulation if it is agreed

[11] Council Document 12124/08, 'Model Articles of association of an SPE' (July 23rd 2008)
[12] Interviews with WP representatives

upon, but it is important that it provides a certain depth. If the Regulation is to be complemented substantially by different national laws it no longer provides uniformity and sufficient predictability for shareholders. The same problem occurs if provisions likely will require the ECJ to interpret their contents. In order to become a popular choice for small business in Europe the Regulation needs to be clear and concise. Predictability is also important for the availability of SPEs, as an unreliable company form is less available to smaller business (subsection 4.3).

4.2.3.2 Confidence

The watering down of the Regulation compromises legal certainty, a big problem with foreign companies operating through branches. It is too early to say whether, or to what extent, an SPE will be able to operate abroad through a branch, without becoming subject to the law of the branch Member State, however some European case-law indicate it must.[13] Courts often have trouble relating to the company law that branches are subject to, making it hard for different stakeholders (even customers) to predict their legal situation.

This is a problem for the UK Limited companies in countries like Germany and Norway, where it has somewhat of a bad reputation. It remains uncertain whether the Working Party will be able to find the necessary common ground to make the Regulation comprehensive enough to gain general trust. The conceptions of SPEs are also important to the availability of the company form (subsection 4.3). If SPEs are not considered trustworthy, they are simply not an option for serious businesses.

4.3 Making the SPE Available

4.3.1 Appealing to a Large Audience

The actual use of the SPE within Europe will be of importance. If the SPE becomes a popular choice for entrepreneurs and smaller business in the future it is likely to reflect that

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[13] Cartesio (ECJ C-210/06) has brought some doubt to this assumption. It lets Member States disallow companies to be registered with them without conducting business in the Member State. Regardless, the Centros line of judgements (ECJ C-212/97...) remains in effect. The issue of SPE branches is of great concern to the Working Party negotiations.

there is a need for such a company form today. In comparison, the European Company is known as somewhat of a disappointment, with only 383 established companies as of July 2009.[14] The SE is often perceived as a company form that failed due to the extensive political compromises it took to pass the Regulation, and many fears the same will happen to the SPE. In any event, to be successful the SPE needs to gain ground in Member States, preferably (in accordance with the Commission's intentions) with entrepreneurs.

A not unlikely alternative is that the SPE, providing at least a uniform set of rules, does not appeal to entrepreneurs, but still gains ground with larger companies establishing subsidiaries in Member States. For companies expanding through subsidiaries, the SPE could provide significant cost savings, making it a likely choice of legal form. Out of the 56% of companies in the EBTP survey saying uniform rules would be useful to them, 61% believed creating a subsidiary in the form of an SPE could result in a cost saving for the company. In other words, the SPE might very well end up a tool for larger enterprises establishing subsidiaries, although originally intended to fit the needs of SMEs.[15]

4.3.2 Availability to Domestic Business

The memorandum states: 'The proposal aims to make the Single Market more accessible to SMEs by providing them with an instrument that facilitates the expansion of their activities in other Member States'. The Commission has a clear intention to stimulate to more cross-border business. In order to succeed in this the SPE needs to be available for companies that are not yet cross-border, enabling them to later expand internationally without having to relate to a completely new legal system.

This is why there is no cross-border requirement in the initial SPE proposal. Having only 8% of SMEs operate in more than one Member State, a cross-border requirement would

[14] Latest figures from the European Company Database (http://tinyurl.com/yfkuuf9, accessed 18.11.2009)

[15] Although not always clearly spoken, it has always been the intention that the SPE facilitate larger businesses, who are more likely to adopt the legislation quickly to form subsidiaries. This could facilitate enough practice of the SPE Regulation for it to become predictable and trustworthy. Still, SMEs are stated as the most important target of the legislation.

prevent the SPE from appealing to 92% that might have good future use of the Single Market. The further implications of a cross-border requirement are not within the scope of this article and will not be covered in the following.

4.4 Concluding Remarks

To prove successful the SPE must overcome several challenges ahead. Most important is that the Working Party ensures the final Regulation is attractive and available to European companies. In the following this article will refer to these success criteria by commenting on provisions' ability to increase the legislation's attractiveness (4.2) and availability (4.3). These are the primary components of this article for analysing the SPE's possible provisions and their appropriateness.

In summary, to harmonise with the criteria above the Regulation should be practical and provide for an easy and cost-efficient way of forming and running a company. It is adamant that the Regulation provide flexibility. It should be investor friendly by allowing shareholders to decide themselves how to conduct their business; yet constraints protecting creditors and minority shareholders should be in place in order for the SPE to gain general trust as a legal instrument. Finally, the Regulation should not leave too many issues to national applicable law as it might create legal uncertainty and elude trust.

5 Company legislation subject to analysis

5.1 The 2nd Council Directive on Company Law

The 2nd Council Directive (77/91/EEC) (2nd Directive) was adopted in 1976. It seeks to harmonize Member States' national law regulating public limited liability companies. More specifically the Directive regulates the maintenance and alteration of public companies' capital. The 2nd Directive illustrates what capital maintenance legislation Member States have previously agreed upon.

It does not constitute a complete legislation; rather it poses minimum standards from which Member States may differ by demands exceeding those of the directive. The actual capital maintenance requirements for public companies are usually stricter than those of the Directive, depending on the Member State in which the company chooses to domicile. Some 2nd Directive provisions resemble the SPE's to the extent that it likely served as a model system for parts of the SPE Regulation.

5.2 The UK Private Limited Liability Company (Ltd)

The company form subject to this article in the United Kingdom is the Private Limited Liability Company (Ltd) where shareholders' liability is limited to their invested capital. Private limited companies may not be offered to the public, separating them from the public limited companies which are subject to a stricter capital maintenance regime. Ltds are primarily regulated by the Companies Act 2006 (CA 2006) which has been fully in place since October 1st 2009, lessening the administrative burdens of the former Companies Act 1985 (CA 1985).

UK capital maintenance regulation on private companies is quite liberal in comparison to other European countries, enabling companies to regulate their business thoroughly in their articles. In the UK system creditors mostly rely on contractual protection, and the lack of a minimum share capital requirement makes the Ltd attractive to European businesses, even more so after the reform of the private companies with CA 2006.

5.3 The German Private Limited Liability Company (GmbH)

The German company form subject to this article is the Gesellschaft mit beschränkter Haftung (GmbH). It is among the most popular company forms in Europe, with estimates showing there are approximately 1 million GmbHs registered.[16] It is regulated by the GmbH-Gesetz (GmbHG – Limited Liability Companies Act) which was revised by the MoMiG (Law for the Modernization of the GmbH and to Combat its Abuse), which liberalizing changes took effect as of November 1st 2008.

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[16] 2007-estimates counted approximately 1 million: Kornblum, 'GmbH-Rundschau', (2008) 99(19) GmbHR.

The GmbH is not designed for public listing and requirements related to formation and operation are much less rigid than those of the Aktiengesellschaft (Stock Corporation). The GmbHG demands a high share capital, but provides flexibility to companies by allowing them to organize themselves quite freely (not considering their strict workers participation regime). Most provisions are non-mandatory and may be deviated from in a company's articles.

5.4 The Norwegian Private Limited Liability Company (AS)

In Norway the private limited liability company is called Aksjeselskap (AS). It is regulated by the Private Limited Liability Companies Act (PLLCA) which took effect as of January 1999. The Norwegian legislation provides an interesting perspective on capital maintenance from a Scandinavian country emphasising legislative creditor protection. It is not as widely used as the other use-case company forms, but more than two thirds of the AS' are owned by only one or two shareholders,[17] making it a typical company for entrepreneurs and SMEs.

5.5 The European Private Company (SPE)

The European Private Company's provisions are still subject to negotiations. As a result this article will seek to depict the different provisions that are likely to be agreed upon. It will present the Commission's initial proposed provisions, the European Parliament's proposed amendments, and the various solutions suggested in the Working Party. In doing this the initial proposal gets the most attention as it stems from a publicly available document. The equally available Parliament amendments and the material on the negotiations in the Working Party gathered through interviews (and a compromise proposal from December 11th 2008) are subject to roughly equal treatment.

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[17] According to Statistics Norway 54% of stock corporations are owned by one shareholder, and another 22,4% are held by two shareholders (http://tinyurl.com/yfs4whb, accessed 18.11.2009).

PART II

6 Structure of capital

6.1 The 2nd Directive

Each share must have a nominal value, but there may be various share classes with different rights attached to them. Even redeemable shares may be issued. A company may not subscribe for shares in itself.

The Directive requires public companies to have a minimum subscribed capital of € 25,000 (Art 6 (1)). The subscribed capital may be paid up in cash or in kind, but not by an 'undertaking to perform work or supply services' or other means that can't be economically assessed (Art 7). At the time the company is incorporated or authorized to commence business at least 25% of the shares' nominal value must be paid up (Art 9 (1)). When shares are issued for a consideration other than in cash, this consideration must be paid in full within five years of that time (Art 9 (2)).

For considerations in kind an expert's report must be drawn up evaluating the asset contributed (Art 10). However, this requirement is subject to narrow modification where 90% of the nominal value of all shares is issued to one or more companies for a consideration other than in cash, and certain other requirements are met (Art 10 (4)).

6.2 The Ltd

There is no minimum share capital requirement for the Ltd, but all shares must have a fixed nominal value (CA 2006 s. 542 (1)). Shares may be denominated in any currency and different share classes may be denominated in different currencies (s. 542 (3)). The types and denominations of share capital are freely chosen and regulated by the company's articles.

Shares may be issued non-, partially or wholly paid for. If the shares are to be paid for, consideration is accepted in cash or in kind (e.g. goods, services, good-will and know-how), s. 582 (1). For non-cash consideration no enquiry or expert report on valuation is required to ensure equal value to the shares. Furthermore, there is no requirement for when the payment needs take place, enabling non-payment or successive payment for shares.

Shares issued at a premium to their nominal value will result in the premium being transferred to a share premium account (s. 610 (1)). This account is treated as share capital and may only be reduced according to the provisions on capital reductions. Still, certain expenses and uses of this account are allowed, e.g. expenses related to the share issue or paying for new bonus shares (s. 610 (2)-(3)).

6.3 The GmbH

Only one subscriber is necessary to incorporate a GmbH, which has legal personality (GmbHG ss. 1 and 13). The amount of share capital, number of shares and their nominal amount must be stated in the articles of association (s. 3 (1)). The minimum share capital of a GmbH is € 25,000 (s. 5 (1)). Half of this must be paid up prior to the company's incorporation (s. 7 (2)). However, with the MoMiG, shareholders may incorporate an *Unternehmergesellschaft (haftungsbeschränkt)* (UG – an entrepreneur company) in accordance with GmbHG s. 5a.

The UG is a form of GmbH which only requires a share capital of € 1 – 24,999 upon incorporation. It is fully regulated by the GmbHG, only differing by (i) its name must contain 'Unternehmergesellschaft (*UG*) haftungsbeschränkt', (ii) each share must be paid in full in cash before registration and (iii) it must save 25% of its annual profits for accumulation until its share capital have reached € 25,000. At that point the UG will become a regular GmbH and may amend the 'Unternehmergesellschaft haftungsbeschränkt' addendum to its name into 'GmbH'.

The minimum nominal value of each share is 1 euro (s. 5 (2)), euros being the only denomination for share capital and shares since January 1st 2002. Each shareholder may hold any number of shares (s. 5 (2)), contrary to the requirement prior to the MoMiG that they only hold one share each.[18] Shareholders are liable to the GmbH if they do not pay the par value for their shares (s. 9).

The articles must expressly allow for contributions in kind. Such contributions must be evaluated in a special report that is published (s. 5 (4)), and they must be delivered or transferred in full prior to a GmbH's application for registration. There are provisions protecting against hidden contributions in kind by means of loans or contracts between a company and its shareholders, prohibiting shareholders from bypassing their obligation to contribute in cash.

Restrictions on the transfer of shares may follow from the articles of association. However, new restrictions might require the consent of all shareholders affected, as such restriction may involve an increase in the obligations of the shareholders (ss. 53 (1) cf. 53 (3)).

6.4 The AS

An AS must have a minimum share capital of NOK 100,000 (approximately € 12,000) (PLLCA s. 3-1 (1)). This share capital must be paid in full before a company is registered (s. 2-11). The capital is divided into one or more shares, whereas each share must have an equal nominal value. A company cannot subscribe for its own shares. Shareholders may be any actual person or legal entity, foreign or national. Only one shareholder is required.

Shares may not be issued at a discount to their nominal value (s. 2-12 (1)), but premiums are allowed. For shares issued at a premium a non-distributable reserve shall be established that may only be used to cover expenses of capital increases, increasing share capital and

[18] GmbHG uses the term 'Geschäftsanteil' and translating this directly to 'share' is imprecise, although the same principles apply.

covering losses that cannot be covered by other equity (s. 3-2). In order to use the reserve for other purposes a company must follow the same procedure as for capital reductions.

Consideration in kind is allowed, but the asset used as consideration must be available for balancing (s. 2-4). Intangible assets are subject to strict requirements in order to serve as consideration in kind. Future work contracts and services are not permitted as consideration. Conversion of debt from past work or services is however permissible consideration, as well as other debt.

6.5 The SPE

6.5.1 The Commission's Proposal

An SPE may issue ordinary or priority shares, which rights are subject to its articles of association. If the articles allow for it, redeemable shares may be issued.

Amendments of the articles changing the rights attached to a class of shares require the consent of a qualified majority of the voting rights attached to the affected shares (COM (2008) 396 Art 14 (3)). No restriction or prohibition on the transfer of shares can be made by amendment of the articles without the affected shareholders' consent (Art 16 (1)). Squeeze-out and sell-out rights are not provided by the Regulation, but may follow from the articles of association.

The minimum share capital of an SPE is € 1 (Art 19). The capital must be fully subscribed and divided into shares, but does not need to be fully paid on issue. The shareholders may decide to allow for any consideration for the shares in the articles of association, even future work and services. The articles may also state that an expert evaluation of considerations in kind is required, although this too depends on the shareholders (Annex I).

SPEs in Member States without the euro may express their capital in their national currency; otherwise it is to be expressed in euro (Art 42 (1)). If a company in a non-euro Member State uses euro for its annual or consolidated accounts the Member State may require that they prepare and publish these accounts in the national currency as well (Art 42 (2)).

6.5.2 The European Parliament's Proposal

Amendment 33 proposes that the minimum share capital may only be € 1 if the articles of association require the management body to sign a solvency certificate guaranteeing the liquidity of the company for one year. Otherwise the capital must be at least € 8,000. It remains unclear whether those signing such a certificate may be relieved of its guarantee upon increasing the company's share capital to € 8,000 if it originally chose to be formed with a capital of only € 1. This might represent a threat to creditors that considered the solvency certificate a prerequisite for entering into a contract with the SPE. The likely solution would be that creditors that entered into contract with the SPE prior to the increase of its capital may hold the company to its solvency declaration, whilst future creditors may not, unless the SPE has given them grounds to assume that the certificate still applies. In case of insolvency this is of importance in order to determine towards whom the management body faces liability.

Amendment 34 provides that a shareholder shall pay in cash the remainder of the value between her acquired shares and a consideration in kind. The claim to payment shall lapse eight years after the company's registration. The SPE's claim to payment given in Amendment 34 does not appear to apply to considerations in kind in general; rather it seems to be valid only for consideration that falls short of the nominal value of the acquired shares. Either way, a payment deadline of eight years is not very strict, especially seeing that an SPE might be free to have a capital of as little as € 1. And even with the Commission's proposal a shareholder may not be relieved of her obligation to provide agreed consideration for shares, unless a capital reduction takes place (Art 20 (2)).

Amendment 60-61 proposes for non-euro Member States that all SPEs shall express their capital in euro in addition to their national currency, and that the preparation and publishing of their annual or consolidated accounts be expressed in both national currency and euro. If the Member State in question allows for companies to express their capital and accounts in euro only, the Amendment does not require them to also use the national currency.

6.5.3 The Working Party on Company Law's proposal

The negotiations on an SPE's share capital have been substantial in comparison to other capital maintenance issues, particularly due to the controversy of the minimum share capital requirement of only € 1. From the latest compromise proposals and the negotiations it appears that the minimum share capital will be a given sum within the interval of € 1-5,000 or € 1 – 8,000, set forth by the Member State in which an SPE is registered.[19] Judith Fischer believes the cap will be closer to € 8,000. With countries like Germany, Austria, and Denmark advocating that a high minimum share capital is necessary; such a compromise has proven necessary. The majority of the Member States would however have supported the Commission's proposed € 1.

The Working Party has reached agreement that 25% of the share capital shall be paid up front of a company's incorporation (Compromise Art 21 (1)), similar to the 2nd Directive Art 9 (1). In addition there should be a time limit to the remaining payment on agreed consideration for shares.[20] In the Compromise Art 21 (1) this time limit was 5 years. In today's text consideration must be made whenever management demands, or at the latest within 3 years from its promise (the time of incorporation or capital increase).[21] Leader of the negotiations, Rolf Skog, explains final discussions may alter the share capital requirements, but states that 'if the Regulation is passed, the interval solution is the most likely choice'.

As for considerations in kind, the 2nd Directive Art 7 prohibits considerations in the shape of work and services (Finland and Italy fought for this to be allowed for the SPE). The Working Party considered leaving it to applicable national law to lay down a potential prohibition. Yet, in the interest of uniformity it was decided that work and services shall

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[19] Interviews with Brian Wessel (08.10.2009) and Judit Fischer (09.10.2009)
[20] Interview with Brian Wessel (08.10.2009)
[21] E-mail correspondence with Judit Fischer (09.11.2009)

not be allowed at all as consideration for shares (Compromise Art 21 (2)). Additionally, consideration in kind will have to be provided up front and in full.[22] This represents severe restrictions on considerations in kind compared to the Commission's proposal.

There will not be a solvency certificate requirement upon registration of a company, as suggested by the European Parliament. No member states are advocating such a demand, except in relation to distributions (see below).

6.6 Concluding Remarks on Structure of Capital

6.6.1 Creditor Protection

The SPE appears to be closest to the Ltd concerning capital structure regulation. Its minimum share capital is low, although it might be increased to € 1 – 8,000. This enables entrepreneurs with viable business ideas to access the legal form without substantial start-up capital, making it more attractive to SMEs (subsection 4.2). Providing € 12,000 for an AS or even € 25,000 for a GmbH might be very difficult for smaller businesses. Even Germany appears to have learned from having several UK Ltds operating solely in Germany, and have now introduced the UG allowing for limited liability without substantial share capital.

However, the UG limitations on distributions and requirement to increase the capital might keep investors from choosing the legal form. Recent studies suggest that smaller business select their legal form only on the basis of formation costs, ignoring costs related to the operation and structure of the company.[23] This would imply that a low minimum share capital requirement will make the SPE more attractive to smaller business (subsection 4.2). Regardless, it will certainly make the company form more available (subsection 4.3).

The minimum share capital of SPEs will not provide for any substantial protection of creditors, especially seeing that it will likely be quite low. Although subject to debate,

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[22] Interview with Judit Fischer (09.10.2009)
[23] Becht, 'Where Do Firms Incorporate' (2006) 70 ECGI - Law Working Paper

many would argue even a high share capital requirement would not offer any creditor protection, rather it would tie up liquid assets which could be put to better use.[24] It is beyond the scope of this article to offer an opinion on this matter, other than to state that the SPE will not offer substantial protection of creditors through a high mandatory share capital. Hence, creditors looking to get involved with SPEs protect themselves the best by means of contract.

The SPE's solution concerning considerations in kind will be closer to that of the 2nd Directive than originally proposed, as work and services may not serve as such consideration. The SPE will also require that 25% of the shares are paid up in front of its incorporation, the minimum requirement of the 2nd Directive and half of the requirement of the GmbHG. However, the SPE once again resembles the Ltd by not requiring an auditor's report on evaluation of considerations in kind (contrary to the requirements of the 2nd Directive, GmbH and AS), and otherwise making considerations in kind easily available.

By not posing as many demands as the GmbHG or PLLCA the Regulation will be more accessible to smaller business (subsection 4.3). Many businesses do not have the competency or money to start a company which requires them to hire an auditor or ensure that considerations in kind are valued perfectly. As a result, they are often forced to opt out of establishing a limited liability company. The SPE Regulation could offer a reliable alternative for these businesses, like the Ltd has in many EU countries.

The development towards the 2nd Directive gives the Regulation a little less edge, but in return it provides creditors with a more familiar capital regime which may result in the SPE being more trustworthy. Shareholders still have sufficient flexibility providing capital for their company, perhaps especially important to attract entrepreneurs and SMEs (subsection

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[24] For a more elaborate discussion on this, see Armour, 'Legal Capital: An Outdated Concept?' (2006) 7(1) EBOR and Rickford, 'Reforming Capital: Report of the Interdisciplinary Group on Capital Maintenance', (2004) 15 EBLR.

4.2). A predictable and easy-to-satisfy capital regime allows start-up companies to be efficient and have low costs related to the initial development of their business.

6.6.2 Investor Protection

Upon incorporation investors that are in disagreement with other future shareholders have the option of demanding better terms or not to invest. Investor protection is more relevant to the situation of investors after incorporation. It should primarily protect against dilution and false premises from the time of incorporation. As a result, investor protection is more relevant to the following sections of this article. Still, the movement towards slightly more conservative capital requirements resembling the 2nd Directive deserves attention.

Moving towards heavier regulation than that of the Commission's initial draft (e.g. by not allowing for work and services as consideration) provides for a certain amount of minority investor protection. Minority shareholders will not have to fight difficult evaluation of considerations, and some commitment must be showed by every shareholder as 25% of payments must be made prior to incorporation. These capital structure provisions may be set out to protect creditors, but in fact offer some protection of investors as well.

7 Capital Increases

7.1 The 2nd Directive

An increase in the company's capital is decided upon by the general meeting. Such a meeting or a company's articles of association may also authorize an increase up to a maximum amount within a period of maximum 5 years (Art 25 (1)-(2)). Where there are several classes of shares, such decisions shall be put to a separate vote at least for each class affected.

Articles 26-27 state the same rules for consideration and when payment's due as for the initial subscribed capital, 25% required up-front payment of the nominal value, premium shares must be paid in full, consideration in kind must be paid within 5 years and is subject to an expert evaluation report.

Capital increases must not take place in violation of pre-emption rights, shareholders are to be offered a *pro rata* part of the new shares issued. This is however subject to certain exceptions in Art 29.

7.2 The Ltd

A limited company may allot new shares to bring in more capital (s. 617 (2) (a)). For companies with only one class of shares the directors may allot such shares unless prohibited by the company's articles (s. 550). Companies with several share classes may allot new shares as long as they're authorized to do so by the company's articles or an ordinary shareholder resolution (s. 551 (1)). Unless pre-emption rights are excluded by provision in the company's articles, existing shareholders often have a right to be offered the shares first (Part 17 Chapter 3). There is no cap on the number of new shares that may be issued.[25]

A limited company may also issue redeemable shares provided that there are other non-redeemable shares in issue and that the company's articles allows for the issue of redeemable shares (s. 684). Shares may not be redeemed unless they are fully paid (s. 686 (1)).

7.3 The GmbH

An increase of the share capital requires an amendment to a company's articles of association. That requires a shareholder resolution favoured by a ¾ majority of the shares represented (s. 53 (2)), unless the articles state a stricter majority requirement. For contributions by the shareholders the requirements are the same as for the initial issue of shares. The amendment of the articles must be filed with the Commercial Register (s. 54).

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[25] With CA 1985 companies needed a stated authorized amount of capital, prohibiting further issue of shares when this maximum amount was met. This requirement was abolished with CA 2006.

It must specify the particulars of both the increase and its consideration, especially if contributions in kind are allowed (s. 56).

For increases from company reserves a shareholders' resolution must be based on a balance sheet supported by an unqualified audit certificate (s. 57c). The articles may additionally allow for the managing directors to increase the capital with an amount less than half of the issued capital at the time of the authorization, within five years of such a decision (s. 55a – *Genehmigtes Kapital*).[26]

Particular pre-emption rights may be given by the articles of association, otherwise a shareholder may grant pre-emption rights to her shares by agreement with a third party. If the articles do not mention pre-emption rights they may be derived from the principle of equality.[27] A shareholders' resolution to increase capital through shareholders' contributions without pro-rata subscription rights requires a majority of the shares, as set forth by the law (75%) or articles of association (higher), and must be made with good reason. For increases from reserves all shareholders participate pro rata to their shares.

Redeemable shares may be issued if the redemption of shares is allowed for in the articles of association. If redemption is to be possible without a shareholder's consent the conditions of such redemption must be expressed clearly.

7.4 The AS

Decisions to increase the share capital is made by the general meeting upon suggestion by the board and may only be made after the company is registered in the Companies Register (s. 10-1). Such a decision must state the amount or interval of the increase, the nominal value of the shares, consideration to be paid and more (s. 10-1 (2) no. 1-9). Furthermore, a capital increase requires an amendment of the company's articles, which can only be made by a qualified majority decision of the general meeting.

[26] Previously only possible for public companies, the rule resembles the one of Aktiengesetz s. 202 (1) and (2)
[27] Schmidt (2002) § 37 V 1. (a) (ee)

The general meeting may also, with a qualified majority decision, provide the board with the power to increase the share capital (s. 10-14). Such a decision may only allow for an increase by an amount equal to half of the current share capital or less, and the power to perform such an issue can last for a maximum period of two years. Also, a company may increase its capital from their distributable profits or premium reserve, once again subject to a qualified majority decision by the general meeting (s. 10-20).

Shareholders have pre-emption rights when new shares are issued, *pro rata* to the amount of their currently held shares. The board may suggest the general meeting waive pre-emption rights, which requires a qualified majority decision (s. 10-5). Even without such a suggestion, the general meeting may waive pre-emption rights if all shareholders affected consent to it.

All new shares must be paid in full, and the increase must be registered with the Companies Register, before the shares are considered issued. Such payment must be confirmed by an auditor (ss. 10-10, cf. 10-9). For consideration in kind another auditor's report is necessary confirming the value of the asset in question, and it must be possible for the asset to appear on the company's balance sheet (s. 10-12).

7.5 The SPE

7.5.1 The Commission's Proposal

The procedure of a capital increase is up to the SPE and must be described in its articles of association. Pre-emption rights are not provided by the Regulation, but may follow from the articles. The decision to increase the share capital must be made by a shareholders' resolution where a majority (as defined in the SPE's articles) of the shareholders favour the increase (Art 27 (1) (h) cf. (2)). Shareholder resolutions do not require the organization of a general meeting, as long as all shareholders are on notice of the decision proposal and the resolution is recorded in writing (Art 27 (3)). Copies must be sent to all shareholders.

The Regulation does not restrict the issue of a new class of shares through a capital increase. The mere offering of new shares of an existing share class would require only a simple majority decision. However, if such an issue constitutes a 'variation of rights attaching to shares' under Art 27 (1) (a), the resolution to increase capital would have to be made by a qualified majority of the shareholders. There are numerous ways in which a share class may be affected by the creation of another share class, e.g. by introducing the right to veto decisions or new preference rights to dividends. For such events the Regulation should be interpreted so that it provides protection for minority shareholders.

If the articles of an SPE do not give shareholders pre-emption rights, a simple majority shareholder may increase the capital herself, in effect watering down everyone else. This could provide the majority shareholder with a qualified majority of the shares, making the minority protection on matters mentioned in Art 27 (2) fictional. It is therefore peculiar that the Regulation neither provides pre-emption rights or a qualified majority requirement for all decisions to alter the share capital.

7.5.2 The European Parliament's Proposal

Amendment 42 suggests that a decision to increase the share capital of an SPE shall require a qualified majority. This strengthens the protection of minorities against dilution. Unless shareholders have equal pre-emption rights, which only the articles may provide, the protection of minorities is very low with the Commission's proposal. The Amendment represents an important safeguarding of minority shareholders, preventing the bypassing of the Regulation's Article 27 (2) on when qualified majority decisions are required.

7.5.3 The Working Party on Company Law's Proposal

Most of the capital increase regulation appears to be left to an SPE's articles, making the final Regulation on this matter much like the Commission proposed. On the matter of majority requirements the Compromise's Art 28 (2) cf. (1) (g) requires a qualified majority as set out in the articles of association for a decision to increase capital. The majority must not be less than two-thirds of the total voting rights attached to the shares issued by the SPE. The current text (as of autumn 2009) also has this requirement.[28]

7.6 Concluding Remarks on Capital Increases

7.6.1 Creditor Protection

The increase of a company's capital does not usually pose a threat to creditors, as it will increase the assets of the company, providing creditors with better coverage for their claims. Creditors with shares in a company providing particular rights, might be subject to provisions on investor protection. As creditors however, they must protect their potential interests of refusing a capital increase by means of contract.

7.6.2 Investor Protection

Minority shareholders often have interests at stake upon a capital increase, e.g. avoiding dilution of their shares or new share classes compromising their rights. The SPE Regulation appears to be focused primarily on providing easy access to capital increases, by leaving most of it to its articles. Yet, a decision to increase capital requires a qualified majority decision. This makes an SPE flexible to operate and potentially attractive to entrepreneurs and SMEs (subsection 4.2).

Many small start-ups will have angel investors or venture capital funding, making entrepreneurs minority shareholders in their own company. For a company form to be available and appealing to them (subsections 4.2-4.3) it should protect against minorities losing ground, unless they've entered into a contract saying otherwise. It is therefore very important that the current text makes it harder to dilute other shareholders.

The qualified majority requirement of the compromise proposal prohibits abuse of minority shareholders, and still has the SPE provide a flexible way of increasing capital for its shareholders. Otherwise, the Regulation would have been much less protective of

[28] E-mail correspondence with Judit Fischer (09.11.2009)

minorities than all the use-case legislations of this article, likely resulting in a less attractive SPE (subsection 4.2).

8 Capital Reductions

8.1 The 2nd Directive

A capital reduction requires a qualified majority decision by the general meeting (Art 40, cf. Art 30). Where there are several classes of shares the decision must be put to separate votes. The subscribed capital must not be reduced to less than the minimum capital of € 25,000 (Art 34).

Creditors with claims antedating the publication of the capital reduction decision shall have the right to obtain security for their claims, as long as they've not fallen due by the date of publication (Art 32 (1)). Unless the creditor is provided adequate safeguards, to the extent that such safeguards are necessary in regard to the company's assets, the reduction may not take place. Safeguards are not necessary for reductions of subscribed capital which purpose is to offset losses incurred or to include money in a reserve provided the amount of the reserve is less than 10% of the reduced subscribed capital (Art 33 (1)).

Any capital reduction made contrary to these rules will be void, and payments to shareholders may not be made until creditors' claims are safeguarded or dismissed by a competent court.

8.2 The Ltd

An Ltd may reduce its share capital according to Part 17, Chapter 10 of CA 2006. There are two ways for such a reduction to take place. One is through a special resolution (3/4 majority is required) supported by a solvency statement.[29] The other is the traditional way of a special resolution confirmed by the court (ss. 645-651).

Creditors with valid claims pose barriers to the draining of companies' assets, as they may object to capital reductions. However, unlike public companies, the private limited companies are not subject to any requirement that they have an authorized minimum of capital or obligation to act upon serious loss of capital.

If a reduction is to be made supported by a solvency statement each director must state that the company after the reduction will be able to pay off its debts as they fall due within the next year (s. 643 (1)). Contingent and prospective liabilities must be taken into account (s. 643 (2)). Furthermore, the solvency statement must be made available to all eligible members involved in passing a written resolution to reduce the capital at a general meeting (s. 642 (2)-(3)).

For reductions that need court approval creditors are given a right to object, whereas the court will consider if they have adequate safeguards for their claim, and whether they should be secured otherwise (ss. 646 and 648). The court may approve the capital reduction unless it finds it unfair, non-equitable or not in the public interest. In practice this issue is usually resolved by creditors consenting to a reduction or receiving security through a bank guarantee.

8.3 The GmbH

A reduction of a GmbH's share capital requires an amendment of its articles, meaning the decision must be made by a shareholders' resolution with at least ¾ of the votes cast and an application must be filed for registration in the Commercial Register and made public. The shareholders' resolution must be published three times before the reduction takes place, in order to alert the company's creditors (s. 58 (1) no. 1). Creditors approaching the company within a year of the last publication that do not consent to the reduction of capital, must

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[29] A new institute with CA 2006, ss. 642-644

have their claims satisfied or secured before the reduction takes place (s. 58 (1) no. 2). Before one year has passed since the last publication of the resolution, the application for registration in the Commercial Register is not valid (s. 58 (1) no. 3), and the reduction cannot take place with legal effect until it is entered (s. 54 (3)).

Reductions made to offset losses do not require the same publication process and enter into effect immediately (s. 58a). Such reductions must be filed with the Commercial Register within three months in order to be valid.

If a capital reduction is to refund contributions or waive consideration for shares that's still owed to the company, the residual nominal amount of the shares must still make up even euro amounts of at least € 1. Furthermore, unless a capital increase is performed simultaneously with a reduction, the reduction may not result in the share capital falling below the minimum of € 25,000.

8.4 The AS

A reduction of the share capital requires an amendment to the company's articles, requiring a qualified majority decision by the general meeting. If the purpose of a reduction is to offset losses that cannot be covered otherwise, it takes effect immediately when registered in the Companies Register (s. 12-5 (1)). However, this will result in the company being unable to distribute dividends for three years, unless they first increase their capital to at least its previous level.

If the reduction will result in a distribution to shareholders, deletion of the company's own shares or a transfer of money to a reserve, the decision must go through a creditor protection cycle (s. 12-6). First the decision must be suggested or approved by the board, subsequently getting approval by the general meeting, and then it must be sent to the Companies Register within two months of the general meeting. The Register announces the reduction in an electronic publication allowing creditors to object to it within two months.

Creditors with undisputable claims shall be paid before the reduction and those with claims that are disputable or not yet due may demand adequate safeguards for their claim, unless the company's situation implies their interests are not jeopardized by the capital reduction. When two months have passed or all creditor demands are handled the company must send notice to the Companies Register along with an auditor's report confirming that the company's creditors do not prevent the reduction from taking place, enabling the registry to declare the reduction final and for distributions to take place.

8.5 The SPE

8.5.1 The Commission's Proposal

A decision to reduce an SPE's capital requires a shareholders resolution by qualified majority (Art 27 (1) (i)) which is disclosed and made available to creditors. If the purpose of a capital reduction is to offset losses the reduced amount may not be distributed to the shareholders (Art 24 (5)). The procedure for reducing capital shall be described in the articles of association (Annex I).

Creditors whose claims antedate the disclosure may apply within 30 days to the competent court for an order that the SPE provide them with adequate safeguards (Art 24 (2)). Creditors must credibly demonstrate their claims are at stake and that safeguards have not been obtained. The Regulation does not provide a mechanism for resolving disputes between an SPE and creditors without the means of a court, however it is obviously within the power (and often interest) of the parties to settle such matters on their own.

A capital reduction becomes effective immediately when an SPE has no creditors at the time the resolution is adopted or on the 31st calendar day following the resolutions disclosure if no creditor has made an application (Art 24 (4) (a)-(b)). Otherwise it takes effect on the first date on which the SPE has complied with orders of the competent court whether to provide adequate safeguards.

In case of a capital reduction, equal treatment of shareholders shall be ensured (Art 24 (7)), a provision likely meant to protect minority shareholders against capital reductions being used to offer disproportionate distributions. A capital reduction may not be used to circumvent the restrictions on distributions, Art 21-22 apply *mutatis mutandis* (Art 24 (1)).

Redemption of shares leading to a reduction of the company's capital must happen in accordance with the above mentioned procedure. The terms and process of such redemption will have to be regulated by the company's articles (Annex I).

8.5.2 The European Parliament's Proposal

Amendment 38 adds to Article 24 that the share capital must not be reduced to a level falling short of the minimum share capital required by Article 19 (4), which for companies without a solvency certificate would be € 8 000 with Amendment 33.

8.5.3 The Working Party on Company Law's Proposal

Concerning capital reductions, the principles of the Commission's proposal have been kept, but there is no longer a need to go to court for creditors before trying to resolve a dispute with a company (Compromise Art 24 (2)). In addition, the Compromise Art 24 (1) requires that the management body of the SPE shall notify its known creditors directly about the reduction of the subscribed capital. With this, the Working Party has given Art 24 (also in the current text) a resembling content to that of the 2nd Directive's regulation on capital reductions, not far from the Commission's proposal.[30]

8.6 Concluding Remarks on Capital Reductions

8.6.1 Creditor Protection

Requiring adequate safeguards is a common way of protecting creditors against wrongful reductions of capital, especially those in effect being distributions to shareholders. The SPE will in this regard be no less protective than the use-case legislations. The deadline for

[30] Interview with Judit Fischer (09.10.2009), phone conversations with Rolf Skog (autumn 2009)

creditors to make their claim will be significantly shorter than that of the GmbHG, but the SPE must in turn alert all their known creditors upon reductions.

8.6.2 Investor Protection

Furthermore the SPE will require a qualified majority decision in order for capital reductions to take place, protecting minority shareholders against disproportionate payments to shareholders. Equal treatment of shareholders in the same position shall be ensured, as clearly stated in the Compromise Art 24 (7).

This requirement and the adequate safeguards prohibit abuse. The rest of the particulars of a capital reduction are left for the SPE to decide in its articles. By protecting both creditors and investors, yet facilitating easy access to reductions as a tool for SPEs, the legislation will be attractive to smaller business (subsection 4.2). SMEs will be free to reduce their capital without unnecessary bureaucracy as long as it does not compromise investors or creditors.

9 Acquisitions of own shares

9.1 The 2nd Directive

Articles 19-22 handles acquisitions of own shares. Member States may permit public companies to acquire own shares themselves or through a person acting in her own name but on a company's behalf. The acquisitions may not reduce the net assets to a level exceeding what a permissible distribution would and authorisation must be given by the general meeting. Certain exceptions apply for the prevention of serious or imminent harm (Art 19 (2)).

Only fully paid-up shares may be acquired, and the nominal value of the total acquired shares may never exceed 10% of the issued capital of the company. Voting rights attached to the shares are suspended and if the shares are shown as assets in the company's balance sheet a reserve of the same amount, unavailable for distribution, shall be included among its liabilities (Art 22 (1) (a) and (b)).

Member States may authorize redemption of the subscribed capital. Redemption of shares must be permitted in a company's articles and decided upon by a general meeting (Art 35). Only sums available for distribution, or proceeds from a new issue of shares, may be used for redemption purposes, and the shares must be fully paid up (Art 39 (b) and (d)). If the shares are paid by distributable proceeds, an amount equal to the nominal value of the shares must be put in a non-distributable reserve, except in the event of a reduction of the subscribed capital (Art 39 (e)).

Shares acquired in contravention of the Directive must be disposed of within one year; otherwise they must be cancelled (Art 20 (3) cf. Art 21). Lawfully acquired shares must be reported in the company's annual report, which shall contain information on shares held, their number and nominal value, reasons for acquisitions and considerations paid (Art 22 (2) (a)-(d)).

The restrictions on a company's acquisition of its own shares also extend to shares in a company where the public company directly or indirectly holds a majority of the voting rights or exercise a dominant influence. Certain exceptions may be made if the company only indirectly has such influence.

9.2 The Ltd

An Ltd may acquire its own shares provided its articles allow it and the shares are fully paid up and not the only non-redeemable shares in issue (ss. 690-691). The company must finance the acquisition either out of distributable profits or out of proceeds from a new issue of shares (s. 692 (2)). Acquired shares are treated as cancelled and the issued share capital is correspondingly reduced. Where the shares are financed by distributable profits, their nominal value shall be transferred to a capital redemption reserve.

An Ltd may also acquire shares out of capital, unless prohibited by its articles (Part 18, Chapter 5). This requires a special resolution by its shareholders, a statutory director declaration on solvency for a year ahead and an auditor's report. Non-consenting members are given the right to object to the court.

An Ltd may also redeem redeemable shares on the same terms as it acquires own shares, even out of capital in accordance with Part 18 Chapter 5. Such shares are also treated as cancelled and the amount of the company's issued share capital is decreased accordingly (s. 688).

9.3 The GmbH

The GmbHG allows for companies to acquire their own shares as long as they are fully paid up (s. 33 (1)), provided the acquisition can be made without net assets falling below the amount of non-distributable reserves plus the company's minimum share capital (s. 33 (2)). A company's balance-sheet must list own shares as assets, and a non-distributable reserve of the accumulated value of the shares must be established. The same applies to loans given against securities in the company's shares. Acquired shares continue to exist, but the rights attached to them are suspended. Shares may also cease to exist upon redemption, if a company's articles allow for the redemption of shares.

9.4 The AS

An AS may acquire its own shares, but not to an extent beyond which the total nominal value of the shares exceed 10% of its share capital (s. 9-2 (1)). A company's own shares held by its subsidiaries also count towards this limit.

An acquisition of own shares must not result in the share capital less the total nominal value of the company's own shares falling below the required minimum capital of NOK 100,000 (ss. 9-2 (1) cf. 3-1 (1)). Acquisitions must be made from distributable profits after approval by a qualified majority decision by the general meeting (ss. 9-3 – 9-4).

According to s. 9-6 certain exceptions are made to the above mentioned restrictions (e.g. acquiring own shares by gift), but if at any time the total nominal value exceeds 10% of the share capital, shares must be sold or deleted through a capital reduction within 2 years. The same goes for wrongfully acquired shares, however subject to a much stricter deadline of 3 months (s. 9-7 (2)).

If redeemable shares are allowed by a company's articles, the redemption of these shares must be done from distributable reserves in accordance with these rules, and if the shares are to be deleted, following the procedure of a capital reduction.

9.5 The SPE

9.5.1 The Commission's Proposal

The SPE shall not subscribe for its own shares, but it may acquire its own shares within the scope of what is distributable according to Art 21-22 (Art 23). There is no cap on the maximum amount of shares owned, except there shall always be at least one issued share. Shares acquired must be fully paid and their vote and other non-pecuniary rights shall be suspended (Art 23 (2)-(3)). If the shares are cancelled, the share capital shall be reduced accordingly and such cancellation shall be governed by applicable national law ((4) and (6)). Shares acquired in contravention of the Regulation or articles of association shall be sold or cancelled within one year of their acquisition ((5)). The same rules apply *mutatis mutandis* to the acquiring of shares by a person acting on behalf of the SPE.

The articles of association must state whether acquisitions of own shares are allowed, the procedure to be followed and the conditions under which the shares may be held, transferred or cancelled (Annex I Chapter IV). A decision to acquire own shares is made by a shareholders resolution with a majority as defined in the articles of association (Art 27 (1) (f) cf. (2)). It does not require a qualified majority decision.

9.5.2 The European Parliament's Proposal

The European Parliament has not proposed amendments to the regulation of a company's acquisition of its own shares; they are in line with the Commission's proposal.

9.5.3 The Working Party on Company Law's Proposal

The Working Party roughly agrees with the Commission, but proposes two amendments. The Compromise Art 23 (6) clarifies that the contents of Art 23 (own shares) shall also apply *mutatis mutandis* to any shares subscribed or acquired by a subsidiary of an SPE. Furthermore, Art 28 (2), cf. (1) (f) requires that decisions to acquire own shares are made by a qualified majority of the total voting rights attached to an SPE's issued shares, providing some minority protection.

9.6 Concluding Remarks on Acquisitions of Own Shares

9.6.1 Creditor Protection

Regulations on acquisitions of own shares appear to be quite uniform. All the use-case legislations require that shares are fully paid, that rights attached to the shares are suspended and usually that the acquisition is made from otherwise distributable means. By being in sync with other European legislation the SPE Regulation is no less attractive than other alternatives on account of acquisitions of own shares (subsection 4.2).

Creditors have an interest in acquisitions of own shares not compromising a company's solvency. Therefore, the SPE provisions on distributions apply *mutatis mutandis* to such acquisitions. What is otherwise not distributable cannot be used to acquire shares. For creditors it might also be important that the balance-sheet of an SPE does not imply that own shares are a big asset for the company. However, the SPE will be subject to nationally applicable accounting law, including the 4th Council Directive (78/660/EEC) which gives thorough instructions on appropriate accounting.

9.6.2 Investor Protection

The 2nd Directive and PLLCA demand that a company not acquire more than 10% of its issued capital. The SPE will be more flexible, as SPEs may buy as much as all but one share with a qualified majority as set forth in its articles of association. Being mostly in compliance with other European law concerning acquisitions, this provision has caused little controversy in the European Parliament and the Working Party.

For minority shareholders, a percentage cap would have represented a barrier for majority shareholders' ability to have their shares bought by the company. Majority shareholders can potentially demand acquisition of their shares as a way of disproportionate distributing. However, the new qualified majority demand provides some minority protection.

10 Distributions

10.1 The 2nd Directive

In order for distributions to be made companies must satisfy a balance-sheet test. The 2nd Directive Art 15 (1) (a) does not allow distributions to shareholders if on the closing date of the last financial year the net assets … does not exceed the subscribed capital plus those reserves which may not be distributed, unless the procedure for reducing the subscribed capital of the company is followed.

The amount of a distribution may not exceed the amount of profits at the end of the last financial year, plus profits brought forward and sums drawn from reserves available for distribution, less any losses brought forward and sums placed to reserve according to the law or statutes, Art 15 (1) (c).

Interim dividends are allowed if the Member States permit them, however they must be based on interim accounts that prove there are sufficient funds for distribution. The demand that dividends stem from profits still apply (Art 15 (2)).

Wrongful distributions must be returned, provided the company proves the receiving shareholders knew the distributions to be wrongful, or could not in view of the circumstances have been unaware of it (Art 16). This is not a very strict rule. In large public companies with groups of shareholders receiving a wrongful distribution, many shareholders might be in good faith about its legitimacy.

10.2 The Ltd

Distributions are widely defined, covering any distribution of a company's assets to its members, whether in cash or otherwise (s. 829 (1)). Issue of bonus shares, reductions of capital and redemptions or purchase of shares out of capital or unrealized profits are not considered distributions. Nor are distributions in relation to a company's winding up.

An Ltd's ability to distribute is related to a balance-sheet test. A company may only distribute its accumulated realized profits less its accumulated realized losses, not considering previously distributed or reduced capital (s. 830 (2)). However, this should be perceived in light of the companies' ability to return capital to shareholders by means of share repurchases, somewhat limiting the constraint of the balance-sheet test.

A company's articles provide for the power of a company to pay dividends, which may be paid either in cash or in kind. In determining a company's power to pay dividends, reference is made to its last audited accounts, but interim dividends may also be paid under certain circumstances (ss. 837-838).

An unlawful distribution which the member at the time of the distribution knew or had reasonable grounds to believe was wrongful results in liability to repay it to the company, or in case of a distribution in kind, to repay the company a sum equal to its value (s. 847).

10.3 The GmbH

A GmbH may distribute annual profit plus its distributable reserves less loss carried forward, unless the law, articles of association or a shareholders' resolution expressly prohibits it (s. 29 (1)). A company formed as a UG must have 25% of the annual profit go to a capital reserve. Distribution is done pro rata to the shares held by the shareholders, unless the articles give preference rights to certain shares (s. 29 (3)). A distribution may not be made if it affects assets required to preserve the share capital, unless a capital reduction or liquidation has taken place (s. 30 (1)). Share premiums may be returned to shareholders, unless they are required to cover a loss of share capital (s. 30 (2)).

With an expected net profit, interim dividends are permitted as long as they do not affect assets required to preserve the share capital. Once again, UG companies are subject to the restriction that they must leave 25% of their profit to a capital reserve.

Any repayment of capital to shareholders in breach of s. 30 (retaining the share capital) must be returned (s. 31).[31] Shareholders in good faith are only liable if repayment is required to cover the claims of a creditor.

10.4 The AS

Distributions from an AS must comply with the rules regarding dividends, capital reductions, mergers or liquidation (s. 3-6). In principle the ability to distribute relies on a balance-sheet test. However, certain assets on the balance sheet are not deemed reliable and will not be counted among the company's assets in regard to distributable profits.

Annual profits and distributable reserves can be distributed after covering any uncovered losses, goodwill, deferred taxes, non-distributable reserves, credit or collateral given to benefit shareholders and the nominal value of own treasury shares (s. 8-1 (1)).

[31] For a more thorough look at the range and application of ss. 30-31, see Bachner (2009) pp. 131-138.

Also, if the company's equity capital represents less than ten percent of the total balance sheet amount, the company may not distribute dividends. This is to avoid extensive gearing, but dividends may still be distributed as long as creditors concur, following the procedure of a capital reduction (s. 8-1 (2)).

In addition, a company is required to hold an adequate amount of equity considering the risk and extent of its business, also restricting the distribution of otherwise available capital (ss. 8-1 (4), cf. 3-4).

Unlawful distributions shall be returned unless the recipient was in good faith (s. 3-7 (1)). Anyone who participated in facilitating such a distribution, not in good faith, will be jointly and severally liable for its return (s. 3-7 (2)).

Additionally there are procedural provisions to prevent circumvention of the dividend provisions, also protecting creditors and minority shareholders. S. 3-8 relate to contracts between the company itself and its shareholders or stakeholders. Such contracts with a value exceeding 10% of the current share capital of a company require approval of the company's general meeting. Furthermore, s. 3-9 requires that transactions between companies in the same corporate structure are done in accordance with the arm's length principle. [32]

10.5 The SPE

10.5.1 The Commission's Proposal

Distributions require a shareholders' resolution. A distribution means any financial benefit derived from the SPE by a shareholder in relation to her shares (Art 2 (1) (a)). It is subject to a balance-sheet test and may only be made if the assets of the SPE fully cover its liabilities after the distribution (Art 21 (1)). The terms 'assets' and 'liabilities' are subject to

[32] The arm's length principle requires that transactions between a company and its shareholders are made as if they were conducted with an independent third party (http://tinyurl.com/yhtprzn, accessed 18.11.2009).

European and national accounting provisions (i.e. the 4th Directive (78/660/EEC) or Regulation (EC) No 1606/2002). The articles may provide non-distributable reserves.

The articles may further require that the management body signs a 'solvency certificate' prior to distributions, certifying that the SPE will be able to pay its debts as they become due for one year (Art 21 (2)). If such a certificate is required it is to be disclosed. The financial year of the SPE, how it may be changed and whether interim dividends can be paid is subject to the articles (Annex I).

A shareholder who has received a wrongful distribution must return it; provided the SPE proves that 'the shareholder knew or in view of the circumstances should have been aware of the irregularities' (Art 22). Shareholders not acting in good faith are obligated to repay such a distribution. This is slightly different from the requirement in the 2nd Directive's Art 16 where the company must prove the shareholder 'could not … have been unaware of' the irregularity in question. It is not as difficult for an SPE to recover a distribution, it is sufficient that the shareholder should have known that the distribution was wrongful. This is even stricter if one considers that shareholders in a private company are more likely to be aware of the premises for a distribution, than those of a larger public company. It is hard to imagine a bulk of shareholders in an SPE making wrongful distributions *bona fide*.

10.5.2 The European Parliament's Proposal

The European Parliament does not seek to drastically change Art 21 on what is distributable. Amendment 35 adds to the limitations on distributions that the remaining amount of the deposit after the distribution must not fall below the minimum amount referred to in Art 19 (4) which was previously € 1. With Amendment 33 however, the minimum amount poses an additional barrier to those SPEs that did not sign a solvency certificate, requiring them to have a minimum capital of € 8,000.

In Amendment 37 the European Parliament suggests that wrongful distributions should be subject to an objective rule of recovery. Regardless of a shareholder's good faith, distributions made contrary to Article 21 must always be returned to the SPE. This is a strict suggestion, unmatched by any use-case legislation.

10.5.3 The Working Party on Company Law's Proposal

Member States have demanded the initial Art 21 be changed by copying from Art 15 of the 2nd Directive.[33] However, this is none the less a balance-sheet test and in reality it does not represent a big change from the Commission's proposal. It may represent more comfort to Member States since it is a more familiar phrasing. The Compromise Art 21 contains the same as the 2nd Directive's Art 15. So does the current text, except national law on necessary legal reserves, important to calculating what is distributable, will not apply to an SPE. Only statutory reserves required by the SPE Regulation are relevant to calculating the amount available for distribution.[34]

A distribution may not exceed the amount of profits at the end of the last financial year, plus profits forward and distributable reserves, less losses and non-distributable reserves (Compromise Art 21 (2)). If the articles allow, interim accounts may be drawn up to facilitate payment of interim dividends (Art 21 (3)). If so, Art 21 (2) applies, but profits made since the end of the last financial year may also be distributed.

The shareholder right to request a solvency certificate will be given to the Member States, so that such certificates may be required by national law in order for an SPE to make distributions. This was proposed in the Compromise Art 21 (4) and is also present in the current text. In a way this might function as a requirement that an SPE holds an adequate amount of equity back from distribution, somewhat similar to the Norwegian PLLCA s. 3-4. The extent of the directors' liability is subject to applicable national law.

Recovery of wrongful distributions has been a thoroughly debated issue in the Working Party. In the Compromise it was equal to Art 22 of the Commission's proposal. During

[33] Interview with Judit Fischer (09.10.2009)
[34] E-mail correspondence with Judit Fischer (09.11.2009)

discussions autumn 2009 it was proposed an objective rule of recovery for distributions resulting in insolvency within one year. If a recipient could prove the distribution did not cause the insolvency, she would be excused from her liability.[35] The suggestion met firm rejection by some Member States, among them the UK. At present, Art 22 is back to the earlier version of the text, similar to that of the Commission, but there is still some uncertainty as to the final outcome. Rolf Skog believes the burden of proof may be changed a little in the final negotiations, but does not find it unlikely with some sort of extra creditor protection in the event of a company growing insolvent.

10.6 Concluding Remarks on Distributions

10.6.1 Creditor Protection

SPEs must have easy access to distributing profits in order to be a company form of interest (subsection 4.3). With too many restrictions on distributions or rigid liability regulation upon wrongful distributions, the company form will not attract much business. Nonetheless, a final Regulation on the SPE must ensure that directors act diligently and in the interest of the company upon ordering distributions. Such restrictions must at the same time not pose as barriers to legitimate distributions.

Distributions are in all use-case legislations governed by the balance-sheet test in slightly different shapes. It is a familiar and trustworthy test that allows for companies to see what assets they need to keep in order to cover their liabilities. Creditors' main interest is in the company staying solvent, which they need to be in order to pass a balance-sheet test. In that respect, the balance-sheet test provides some creditor protection, although it does not guarantee future solvency.[36]

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[35] Interview with Judit Fischer (09.10.2009)

[36] Jonathan Rickford argues directors should 'provide an adequate prior assurance of solvency', requiring a solvency test: Rickford, 'Legal Approaches to Restricting Distributions to Shareholders: Balance Sheet Tests and Solvency Tests' (2006) 7(1) EBOR.

Future solvency is often more reliant on business strategy than current assets and liabilities. And creditors would want to be protected against excessive distributions leading to future insolvency as well. The solvency certificate which Member States may require upon an SPE's distributions will force directors to take into account prospective liabilities, making companies more likely to withhold an appropriate amount of equity. This provides some extra protection for creditors,[37] but on the other hand it might make companies more restrictive on their distributions, possibly making the company form less attractive (subsection 4.2).

When it comes to recovery of wrongful distributions it remains unclear what the SPE provisions will say. It is likely that at least recipients of distributions in bad faith will be liable for the amount distributed. Compared to the use-cases above this is as good a protection as most of them and it will likely suffice to make the SPE a trustworthy company form (subsection 4.2). An objective rule of recovery for (some) cases of insolvency would strengthen the creditor protection more than what is necessary. European company law appears to recognize that shareholders acting *bona fide* should not be held liable for a wrongful distribution. Compliance with such a principle might be of importance for the SPE to appeal to a larger audience within European business (subsection 4.3).

10.6.2 Investor Protection

Investors need protection from other shareholders receiving disproportionate distributions, e.g. through shareholder loans. It is important that they are given a right to object if transactions or distributions are happening at the expense of the arm's length principle. However, it is within the general duties of the directors to act in the best interests of the SPE (Compromise Art 32). This prohibits distributing or buying of assets from shareholders at a price different from their fair market value, as it would clearly be to the company's disadvantage.

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[37] Wolfgang Schön argues both the balance-sheet and solvency test are necessary to protect creditors: Schön, 'Balance Sheet Tests or Solvency Tests – or Both?' (2006) 7(1) EBOR.

11 Maintaining Capital

11.1 The 2nd Directive

In case of serious loss of the subscribed capital, where the required loss may not exceed 50%, a general meeting of the shareholders must be called to consider whether the company should wind up, increase its capital or take other measures (Art 17 (1)-(2)).

11.2 The Ltd

Directors are required to act in a way that's most likely to promote the success of the company as a whole, and CA 2006 s. 172 lists a series of stakeholders to be considered by directors. Creditors are not mentioned in this list, supporting the general tendency of creditors having to safeguard themselves through contract or other means of blocking company actions that represents a threat to a creditor's claim.

Directors are not law bound to consider creditors' interests when insolvency is merely in prospect, although this was considered in the review of UK company law prior to CA 2006.[38] However, they may be held personally liable if they knew or should have concluded that the company would ultimately go into liquidation, and they failed to take every step with a view to minimizing creditors' loss that they ought to have taken.[39]

11.3 The GmbH

Upon loss of more than half of the share capital a director is law bound without delay to call a shareholders' meeting (s. 49 (3)). For directors of a UG such meeting must be called without delay in case of imminent insolvency.

Directors are obliged to act in accordance with what a prudent businessman would (s. 43 (1)), promoting the interests of the company and its stakeholders. Upon violation of a director's duties the director may become liable towards third parties by means of damage

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[38] White Paper CM 5553-I, 'Modernising Company Law', paras. 3.8-3.14
[39] The Insolvency Act 1986 s. 214

claims. Here the rules as to the 'Vorstände' of an Aktiengesellschaft can be applied vice versa, particularly the business judgement rule.

Directors are especially held liable for payments made in breach of ss. 30 and 33 (s. 43 (3)), a stricter duty of care is required of directors concerning the share capital and own shares.

11.4 The AS

A company must at all times hold an adequate amount of equity considering the risk and extent of its business. If its equity is presumed to be lower than what is reasonable and adequate the board must take immediate action. They shall call a general meeting where they account for the company's economic situation and propose applicable measures or the liquidation of the company (ss. 3-4 and 3-5). The same applies if the company presumably has lost half of its share capital.

11.5 The SPE

11.5.1 The Commission's Proposal

Directors have a duty to act in the best interests of the SPE and risk liability for acts in breach of the Regulation, the SPE's articles or a shareholder resolution (Art 31 (1) and (4)). There is no demand that directors take action upon severe loss of capital or a presumably inadequate equity. However, insolvency regulation is left to national applicable law, allowing for Member States to require directors to take action upon nearing insolvency.

Although acting in the company's interest might appear a superficial duty at best, disloyal behaviour against shareholders may certainly result in liability. Disloyalty towards creditors does not receive particular mention in the Commission's proposal, but liability may incur on grounds of contract even though the Regulation's requirements are met. Penalties and liability will rely on applicable national law (Art 31 (5)).

11.5.2 The European Parliament's Proposal

Amendment 51-52 suggests a different definition of Art 31 (4)-(5), in effect strengthening the demand that directors behave in the interest of the company. Amendment 51 suggests Art 31 (4) be changed so that all directors are 'jointly and severally liable in respect of the company', although the act of failure is not necessarily committed by all of them. To avoid liability, directors must demonstrate their own blamelessness or that they objected and 'made known their disagreement with the failure to fulfil duties'. Instead of requiring 'loss or damage to the SPE', caused by an 'act or omission in breach of his duties', liability is suggested to occur for 'any prejudice to the SPE' which may be derived from 'a failure to fulfil the duties incumbent on them (the directors)', in relation to the Regulation, its articles and shareholder resolutions. This amendment makes it easier for directors to be held liable.

Amendment 52 goes further and amends Art 31 (5) that states applicable national law shall govern the further liability of directors. The amendment suggests that directors be required to pay compensation for breaches of Art 21 (distributions) or Art 23 (2) (acquisitions of own shares). It also states that a requirement for the directors to compensate the company's creditors shall not be waived although the directors acted in accordance with a shareholder's resolution. This amendment would provide a clear provision stating that directors are required to take into account the interests of their creditors. In such respect it might provide for more credibility and trust for the SPE (subsection 4.2).

11.5.3 The Working Party on Company Law's Proposal

By enabling Member States to require solvency certificates prior to distributions the Working Party has added to the requirements of a company's capital. If a distribution will leave the company with an equity allowed for by the Regulation, but insufficient for securing the company's future liquidity, directors will be less likely to sign a solvency certificate. In effect, equity will be held back in order to ensure the proper amount of liquid assets in the company. On the other hand, the liability of directors is subject to applicable national law and may vary. Furthermore, a solvency certificate is not a guarantee, and such certificates are not likely to reflect a safeguard other than proper business being done.

Directors still have a duty to act in the best interests of the SPE (Compromise Art 32), but there are no other formal capital maintenance requirements. Since the capital maintenance regime of the SPE is covered by the Regulation, national laws (posing a duty to act upon serious loss of capital or to hold an adequate equity) shall not apply.

11.6 Concluding Remarks on Maintaining Capital

11.6.1 Creditor Protection

There are no substantial requirements that an SPE maintains capital or acts upon losses of capital except for the barriers posed in the aforementioned regulation of distributions, capital reductions and acquisitions of own shares. This does not necessarily represent less of an obligation for directors to take action when an SPE has suffered a potentially harmful loss of capital or equity. Directors will be required to act in the best interest of their company, which might involve calling a meeting to discuss its economic situation.

The duty to act upon serious loss of capital is not as relevant for companies with a high share capital. An SPE might have a very low capital, unlike a GmbH or AS. When companies are small and have little to no equity the duty to act upon loss of half of their capital makes little sense, and when they grow big such action might follow by it being in the company's best interests. Considering this, the Regulation better facilitates SMEs by not posing this demand (subsection 4.2).

In summary, the non-restrictive SPE regulation of the Commission's proposal enables a flow of capital that does not tie up liquid assets, which is important in order to facilitate SMEs. If solvency certificates end up being required for distributions this will also add to the responsibilities of directors, demanding they really consider distributions to be in accordance with the company's situation and future liabilities. Creditors should be sufficiently covered by this regulation, and if they require additional safeguarding they should resort to the means of contract.

11.6.2 Investor Protection

The duties incumbent on directors to act in the best interests of the company could be seen as protection of the investors' interests. Apart from that, the investors do not hold particular interests at risk protected by the provisions on maintaining capital in the company.

PART III

12 Capital Maintenance Analysis

This section offers a set analysis of the SPE's capital maintenance regime. It will place the SPE's capital maintenance provisions in a comparative perspective with the use-case legislations and offer insights on which interests are safeguarded by the Regulation.

The capital structure of an SPE was originally very flexible and posed little to no barriers to companies. It now offers more familiar demands, in line with the 2nd Directive (e.g. that consideration for shares is subject to several requirements), making it more serious and providing reliability towards an SPE's creditors and surroundings. The Regulation remains quite flexible in terms of capital structure, providing easy-to-understand provisions and freedom to operate with different share classes and a low minimum share capital.

Capital increases, capital reductions and acquisitions of own shares are roughly in line with the use-case legislations. They are made easily available to an SPE by having its articles provide particulars on the processes. All the provisions pose barriers to the draining of a company's assets, but they are easy to employ provided minimum requirements are met (typically that creditors and investors are safeguarded against abuse). Being comparable to solutions of other European company forms the SPE provisions appear trustworthy.

Access to distributions was initially very liberal. It will remain an available and flexible way of distributing assets to shareholders, but with some restrictions from the 2nd Directive. It will be left to Member States to require a solvency certificate, which might pose an additional barrier to distributions. This puts SPEs in line with the more strict European legislations (e.g. the PLLCA) and will make the company form appear more reliable to creditors. However, there is some risk to the solvency certificates posing an excessive barrier to risk-taking, the actual purpose of business.

All in all the amendments made to the Commission's proposal moves the Regulation in a more serious direction. Co-author of the initial proposal, Judith Fischer, expressed in an interview that they wanted it to provoke and cause debate, as they knew it would be emasculated by the compromise process. Hence, the initial proposal was very investor-friendly and without much capital maintenance demands. The later revision has resulted in numerous amendments providing safeguards for creditors and investors which would otherwise be rather unprotected.

Although the capital maintenance provisions have not been in focus as much as other issues, there have still been significant changes made. Overall it seems a more appropriate balance has been struck between having an investor-friendly Regulation and protecting creditors. The minimum share capital will be an amount set forth by the Member States, limited upwards to € 5,000-8,000. Consideration in kind is still allowed without an auditor's report, but may not be paid in work and services. Capital increases can no longer be used to dilute shareholders, and reductions may be made without the help of a court. Distributions are somewhat more restricted, although they still follow the principle of a balance-sheet test. These changes represent not only compromises with Member States with differing capital regimes, but steps towards a more credible corporate entity that may have an easier task of gaining trust.

13 Compliance with Success Criteria

13.1 Capital Maintenance – a Prerequisite for Success?

Capital maintenance provisions cannot reveal whether the SPE will be successful. This relies on the whole Regulation, e.g. whether companies may be formed *ex nihilo* and without a cross-border component. However, capital legislation must not extensively tie up liquid assets and prohibit legitimate business from being done. This section considers if the capital regulation at least does its part to making the SPE successful.

13.2 Will the SPE be Attractive?

As stated in section 4.2 it is of importance that the Regulation is tailored to the needs of SMEs and capable of cost-efficient formation and operation. Considering the analysis of sections 6-12 this article will argue that these criteria are met.

In terms of capital requirements the final Regulation should reflect that entrepreneurs face an entry barrier of formation costs. In order to gain ground it is important an SPE is easily available both in terms of having a low minimum capital and being easy to register. This requires that the Regulation not put up a high minimum share capital demand. The interval of € 1 – 5,000/8,000 is not particularly high and complies with this requirement.

The Regulation should not contain provisions that prohibit a natural flow of capital for SMEs. Distributions of profits should be easily available, but in turn they should not be possible contrary to what's in the interest of the company. Limiting distributions by a balance-sheet test is a good way of doing this, but perhaps not sufficient for high-risk businesses, when considering the situation of creditors, especially tort creditors. The solvency certificate could be a good way of protection, although it would limit the freedom of SPEs. The Regulation enables Member States unfamiliar with the solvency test not to require it. The solvency test will therefore not likely affect the SPE's attractiveness.

Another way of protecting tort and regular creditors would be an objective rule of recovery for distributions that lead to insolvency. It remains unclear what the final solution will be, but it is likely that shareholders in good faith will not be liable for wrongful distributions. Potential tort creditors will still have some protection. In any event, in order to gain ground as a corporate entity, the Regulation should stress predictability for shareholders, enabling them to distribute profits without risking liability after a longer period of time.

13.3 Will the SPE be Available?

As stated in section 4.3 the SPE will have to appeal to a large audience in order to be deemed a success. By being attractive to and really facilitating SMEs the company form could be quite the success. Unless a strict cross-border component requirement or other incorporation-barriers are set forth in the final Regulation, this article will argue that the Regulation will prove a success also in this regard.

SMEs might very well become more competitive with the Regulation, as it does not contain any major disadvantages to other legal forms (although the Ltd is sometimes more liberal). By familiarizing themselves with the SPE legal form, SMEs will be able to expand into more of the Single Market available to them, without significant legal costs. However, they will have to either spend resources on a thorough set of articles of association, unless they employ model articles as set forth by the Member States. The uniformity should also enable companies to use standard documents and procedures for all their subsidiaries. This can give businesses synergy effects as they will no longer have to reinvent the wheel for transactions they've previously prepared.

As the negotiations of the Working Party leaves more and more legislation to applicable national law, there is a serious risk that the Regulation will not provide the necessary provisions for an SPE to be a true European company. If the Regulation becomes far from exhaustive, it will not provide the uniformity and predictability that is often important to entrepreneurs and SMEs, and among the main arguments for why the company form has great potential. It remains to be seen whether the Working Party will be able to find an agreement that allows the SPE's success.

13.4 Concluding Remarks

It is the conclusion of this article that the capital maintenance regime of the SPE will not hinder the legal form from gaining ground. In fact, unless the Regulation requires difficult cross-border components or very rigid employee participation regulation, it will likely be very much of use to European businesses. Whether these are SMEs looking for a way to expand their business or the more resourceful businesses looking to create subsidiaries is too early to tell. Regardless, the SPE at least has the potential to become a serious alternative to national company forms in Europe.

14 Outlook

As the final provisions of the Regulation are not yet subject to agreement in the Working Party, there is a chance it will not be passed at all. The SPE's future is not yet decided as of November 2009. The Commission has expressed that their last attempt to pass the Regulation will be with the Swedish Presidency.[40] The Swedes have their last chance of bringing the issue up at the European Council meeting of December 4th.[41]

Unless they are successful in finding a compromise prior to that meeting, the outlook of the Regulation is grim. The heavier Member States are not showing much interest in passing it and the same conflicts are present today as there were with the initial proposal. Unless Member States are able to agree on a compromise by December 2009, a solution before long is not likely.

Even if the Regulation is not passed there is reason to believe the SPE initiative has had an effect on European SMEs. The discussions on company law for private companies and how to facilitate entrepreneurs and SMEs have created awareness in Member States: that other

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[40] Working Party interviews (2009)

[41] Phone interview with Rolf Skog (24.09.2009)

legal solutions than their own might stimulate to more business being done. In fact, the recent development in European company law is towards liberalising reform, not unlikely because of the initiative shown the last few years on facilitating smaller business in the European Union. As such, the Regulation might still have served its purpose.

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16 List of References

16.1 Regulations

- Treaty establishing the European Community (EC Treaty)
- Second Council Directive 77/91/EEC of December 13th 1976
- Fourth Council Directive 78/660/EEC of July 25th 1978
- Regulation (EC) 2001/2157 of October 8th 2001 (European company (SE))
- Companies Act 2006 (United Kingdom)
- Companies Act 1985 (United Kingdom)
- Insolvency Act 1986 (United Kingdom)
- Gesetz betreffend die Gesellschaften mit beschränkter Haftung (Germany)
- Gesetz zur Modernisierung des GmbH-Rechts und zur Bekämpfung von Missbräuchen (Germany)
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16.4 European Parliament Documents

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16.5 European Council Documents

- Council Document 17152/08, 'Proposal for a Council Regulation on the Statute for a European Private Company (SPE)' (December 11th 2008), http://tinyurl.com/ydpgoja
- Council Document 12124/08, 'Model Articles of association of an SPE' (July 23rd 2008), http://tinyurl.com/ylr9vzy
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16.6 Interviews

Several interviews were conducted for this article in Brussels October 2009. In addition a significant amount of phone and e-mail correspondence was conducted in the period of September – November 2009. Interview subjects include Attaches in the Working Party, national EU delegations and representatives in the Commission, Parliament, Council and Council Presidency. Primary sources of information are listed below.

- Mads Andenæs (Oslo, autumn 2009)
  Professor at the University of Oslo, Author of European Comparative Company Law (2009) and several related articles
- Dr. Sebastian Kuck (Brussels, October 6th 2009)
  European Parliament, the office of MEP Klaus-Heiner Lehne (CDU)
- Bill Jones, phone interview (October 7th 2009)
  Representative in the Working Party on Company Law from the United Kingdom
- Brian Adrian Wessel (Brussels, October 8th 2009)
  Representative in the Working Party on Company Law from Denmark
- Lauri Tenhunen (Brussels, October 9th 2009)
  Representative in Working Party on Company Law from Finland

- Judith Fischer (Brussels, October 9th 2009)
  European Commission, Co-author of the European Commission's proposal and the Working Party on Company Law compromise proposals
- Rolf Skog, phone interviews (autumn 2009)
  Swedish Council Presidency, Desk Officer of the Working Party on Company Law

16.7 Other Documents

- French Presidency Working Programme: http://tinyurl.com/yzzzd3t
- Czech Presidency Working Programme: http://tinyurl.com/yfvzr26
- Swedish Presidency Working Programme: http://tinyurl.com/mdcnh3

16.8 Online Sources

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17 List of Abbreviations

2nd Directive	Second Council Directive 77/91/EEC of December 13th 1976
4th Directive	Fourth Council Directive 78/660/EEC of July 25th 1978
AS	Aksjeselskap
CA 1985/2006	UK Companies Act 1985/2006
The Compromise	Council Document 17152/08 of December 11th 2008
EBLR	European Business Law Review
EBOR	European Business Organization Law Review
EBTP	European Business Test Panel
EC Treaty	Treaty establishing the European Community (TEC)
ECJ	European Court of Justice
ECL	European Company Law
EU	European Union
GmbH	Gesellschaft mit beschränkter Haftung
GmbHG	Gesetz betreffend die Gesellschaften mit beschränkter Haftung
Ltd	UK Private Limited Liability Company
MEP	Member of the European Parliament
MoMiG	Gesetz zur Modernisierung des GmbH-Rechts und zur Bekämpfung von Missbräuchen
PLLCA	Norwegian Private Limited Liability Companies Act
SE	Societas Europaea (European Company)
SME	Small and Medium Enterprise
SPE	Societas Privata Europaea (European Private Company)
UK	United Kingdom
The Working Party	European Council's Working Party on Company Law